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February Machinery Orders

Orders experience m/m decline, but exceed market consensus

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Summary

- According to statistics for machinery orders in February 2015, the leading indicator for domestic capex, private sector demand (excluding shipbuilding and electrical power), were down by -0.4% m/m, while at the same time exceeding market consensus (-2.2%).

- Looking at results by source of demand, the manufacturing industries by +0.9% m/m for the first time in two months. Meanwhile, non-manufacturing orders (excluding shipbuilding and electric power) declined for the first time in four months at -3.6% m/m. However, according to the 3-month moving average, the second consecutive month of growth was achieved. In other words, overall results were not so bad as to correct our basic assumption that orders are still in a growth trend.

- According to the CAO outlook for the Jan-Mar 2015 period, private sector demand (excluding shipbuilding and electrical power) is expected to grow by +1.5% q/q, its third consecutive quarter of gains. This figure is considered to be achievable even if a decline of as much as -6.5% m/m is experienced in March. Hence there are no high hurdles to achieving further growth. DIR sees private sector demand (excluding shipbuilding and electrical power) showing clear signs of a comeback in the Jan-Mar 2015 period with q/q growth seen.

Machinery Orders (m/m %; SA) **Chart 1**

	2014										2015	
	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb
Machinery orders (private sector)*	19.1	-9.1	-19.5	8.8	3.5	4.7	2.9	-6.4	1.3	8.3	-1.7	-0.4
Market consensus (Bloomberg)												-2.2
DIR estimate												-1.5
Manufacturing orders	23.7	-9.4	-18.6	6.7	20.3	-10.8	12.0	-5.5	-7.0	24.1	-11.3	0.9
Non-manufacturing orders*	8.5	0.9	-17.8	4.0	-4.3	10.7	1.7	-7.5	0.5	7.2	3.7	-3.6
Overseas orders	3.2	71.3	-45.9	62.8	-42.6	29.1	-9.4	-4.6	-6.0	-6.9	24.2	8.0

Source: Cabinet Office, Bloomberg; compiled by DIR.
*excl. those for shipbuilding and from electric utilities.
Note: Figures on market consensus from Bloomberg

February orders experience m/m decline, but exceed market consensus

According to statistics for machinery orders in February 2015, the leading indicator for domestic capex, private sector demand (excluding shipbuilding and electrical power), were down by -0.4% m/m, while at the same time exceeding market consensus (-2.2%).

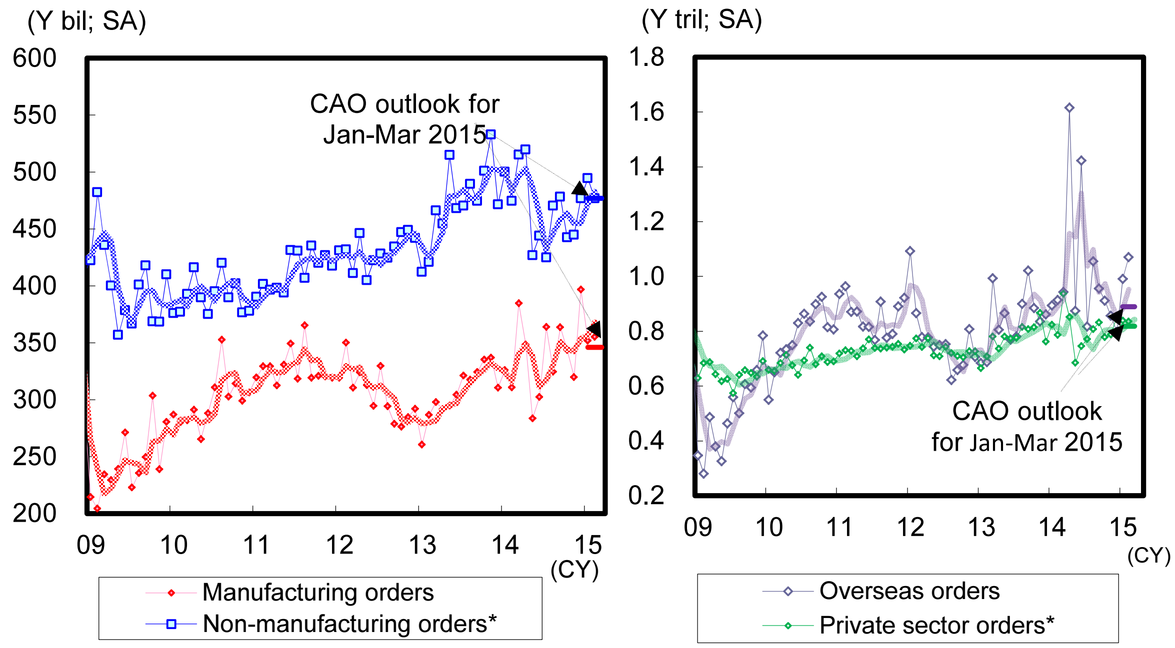
Manufacturing achieves good results seen both in headliners and in performance by industry

Looking at results by source of demand, the manufacturing industries grew by +0.9% m/m for the first time in two months. Orders continue in a moderate growth trend backed by improvements in corporate earnings. Looking at results by industry a wide range of areas posted m/m gains, with especially outstanding results from the following: foods and beverages (+186.1% m/m), chemicals (+25.1%), and automobiles, parts and accessories (+14.1), and other transport equipment (+32.6%). In the case of the foods and beverages industry, considerable gains were likely due to special factors, and hence should be viewed with a certain grain of salt. As for chemicals, these results show that the industry has finally hit bottom after a series of m/m declines, while in automobiles, parts and accessories, as well as other transport equipment, performance finished flat when all was averaged out.

Non-manufacturing posts m/m declines, but averaged out, continues growth

Non-manufacturing orders (excluding shipbuilding and electric power) declined for the first time in four months at -3.6% m/m. However, according to the 3-month moving average, the second consecutive month of growth was achieved. In other words, overall results were not so bad as to correct our basic assumption that orders are still in a growth trend. Results by industry were as follows: wholesale and retail trade (-75.8%), transportation and postal activities (-34.3%), and agriculture, forestry and fishing (-49.7%). As for wholesale and retail trade, the sharp decline in orders is likely a reaction decline after the large-scale shipping related orders received during the previous month. hence no need for pessimism here. Similarly, agriculture, forestry and fishing experienced a rebound after the major growth of the previous month. On the other hand, m/m growth was achieved in some of the non-manufacturing industries, including telecommunications (+32.7% m/m), other non-manufacturing (+5.6%), and real estate (+134.8%).

Orders by Demand Source (seasonally adjusted figures) — **Chart 2**

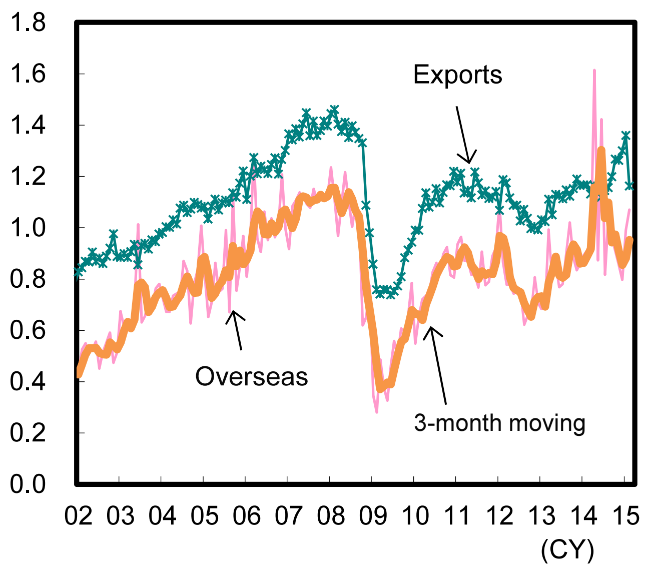


Source: Cabinet Office (CAO); compiled by DIR.
*excl. those for shipbuilding and from electric utilities.
Note: Thick lines 3M/MA basis.

Overseas Orders show signs of a comeback

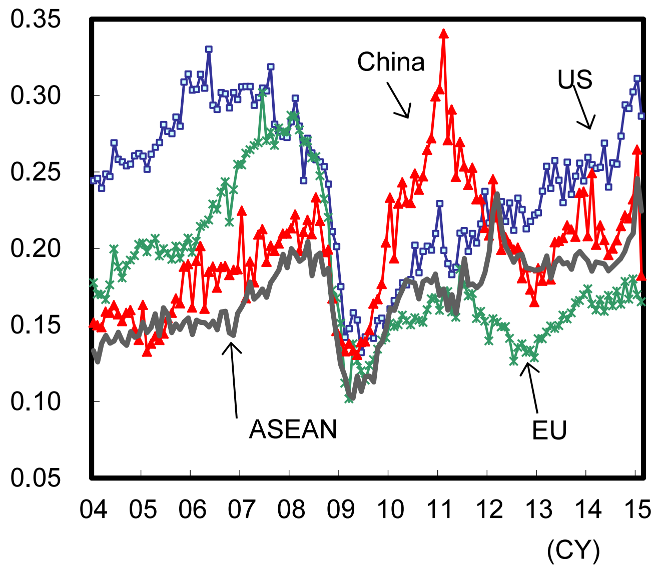
Overseas demand won growth for the second consecutive month at +8.0% m/m in a show of making a comeback. The economic slowdown in China requires caution in the future, but it is the US economic recovery providing the underlying support for overseas demand.

General Machinery: Overseas Orders and Exports (Y tril; SA) **Chart 3**



Source: Cabinet Office, Ministry of Finance; compiled by DIR.
Notes: 1) Exports seasonally adjusted by CAO, general machinery exports by DIR.
2) Thick line for overseas orders 3M/MA basis.

General Machinery: Exports by Trading Partner (Y tril; SA) **Chart 4**



Source: Ministry of Finance; compiled by DIR.
Note: SA by DIR.

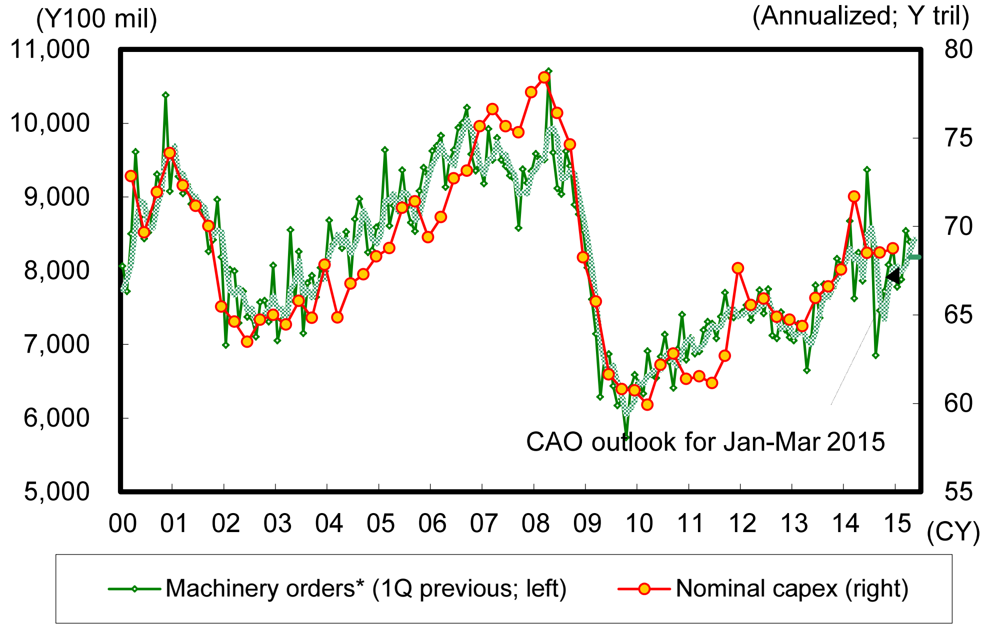
Capex on a GDP basis expected to shift into a moderate growth trend

According to the CAO outlook for the Jan-Mar 2015 period, private sector demand (excluding shipbuilding and electrical power) is expected to grow by +1.5% q/q, its third consecutive quarter of gains. This figure is considered to be achievable even if a decline of as much as -6.5% m/m is experienced in March. Hence there are no high hurdles to achieving further growth. DIR sees private sector demand (excluding shipbuilding and electrical power) showing clear signs of a comeback in the Jan-Mar 2015 period with q/q growth seen.

According to GDP statistics, real capital expenditure fell in q/q terms during the Oct-Dec 2014 period, confirming that capex spending was stagnant. However, the coincident index for capex, shipments of capital goods, is now in a moderate growth trend. On the whole, machinery orders, a leading indicator, are moving upwards, while the BOJ Tankan survey on planned capital spending shows a positive attitude amongst corporations towards capex. In addition, the decline in the price of crude oil will likely provide positive support for growth in capex, as it contributes to improvement in corporate earnings. Hence we believe that capex spending on a GDP basis will gradually move back into a growth phase.

Domestic Demand and Nominal Capex

Chart 5



Source: Cabinet Office (CAO); compiled by DIR.
Note: Excluding those for shipbuilding and from electric utilities; thick lines 3M/MA basis.